Tennessee Housing Development Agency

Report on Incentives for the Development of Affordable Housing

Executive Summary

Pursuant to House Joint Resolution 505, the Tennessee Housing Development Agency was directed to study incentives for the development of affordable housing. THDA was asked to examine inclusionary housing programs in other states, evaluate population and market trends in Tennessee, and recommend, if appropriate, affordable housing initiatives for consideration in Tennessee.

Substantial population growth in metropolitan suburbs and nearby counties in Tennessee has led to increasing demand and rising prices for housing in these local markets. Housing affordable to low-income households is often occupied by others who could have chosen more expensive homes if they were willing to spend up to 30 percent of their incomes for housing. However, the analysis of Tennessee housing occupancy shows that families, in general, have housing costs well below the 30 percent threshold defining affordability. Consequently, many lower income households, competing with those better off than themselves, end up paying more for housing than they can easily afford.

Inclusionary housing, sometimes called inclusionary zoning, is a citywide or countywide program. It either mandates or assigns as a voluntary objective a percentage of housing units in new developments to be sold or rented to lower- or moderate-income households at affordable rates. The report provides detail on inclusionary housing programs in Montgomery County, Maryland, Fairfax County, Virginia, and California. Some of the insights are:

- Inclusionary housing is a local initiative. Its success or failure depends mainly on local political, economic, housing market, and demographic conditions.
- In order to adapt the program to local conditions, the inclusionary housing model allows a variety of choices regarding incentives, requirements, and alternate developer options.
- States have played a pivotal role by encouraging localities to consider affordable housing initiatives and by enabling local governments to adopt necessary ordinances.
- Maintaining affordability of inclusionary housing program units has been a major problem, even though a majority of the programs require that affordability be maintained for 30 years.
- Inclusionary housing programs often allow in-lieu fees, units to be built off-site, and fewer amenities. However, these cost reductions for developers might reduce some of the potential of fostering economic and racial residential integration.

Inclusionary housing programs which made noticeable achievements were developed under the following demographic and market conditions:

- Population density exceeding 1,000 persons per square mile;
- Limited availability of farm land with higher prices; and
- Rapidly increasing home prices and consequent reduced affordability.

Davidson and Shelby are the only Tennessee counties to exceed the above population density threshold. Land is available in Tennessee metropolitan counties at prices much more reasonable than in the areas which pioneered inclusionary housing programs. Home prices exceeding three times median income, a housing market condition found in these other areas, is not as prevalent in Tennessee metropolitan counties (only Williamson County approaches this level of housing cost burden). Shelby, Davidson, and Williamson Counties have recently passed some ordinances that resemble inclusionary housing programs. None of these three programs have produced yet any significant number of affordable units.

Other innovative affordable housing initiatives examined in the report include (1) state construction loan funds; and (2) tax abatement programs.

Generally, the report shows that housing market imbalances and price pressures brought about by rapid population growth have prompted many states and localities to launch initiatives for construction of affordable housing. Some of these initiatives have been successful and provide guidance for other localities. If urban growth continues at current levels in Tennessee, metropolitan housing markets may soon approach similar market conditions and similar initiatives may be warranted.

Incentives for the Development of Affordable Housing in Tennessee

PART I. Summary of the Legislative Assignment

Introduction

In February 1998, the Tennessee General Assembly passed House Joint Resolution 505 (included in the Appendix) directing the Tennessee Housing Development Agency to:

- Study the possibility of offering economic incentives for creating affordable housing as part of any new construction;
- Consider the practicality of mixed income subdivisions;
- Survey other state's efforts, including the involvement of their housing finance agencies;
- Review the success of such programs, and
- Report on a range of alternatives presently being used to provide more affordable housing.

THDA was asked to look at specific models of affordable housing throughout the country including, but not limited to, the following:

- The Montgomery County, Maryland, "Moderately Priced Housing Program;"
- The California State Density Bonus Law;
- The Connecticut Housing Partnership Program or its Regional Fair Housing Compact Pilot program; and
- The Connecticut Affordable Housing Land Use Appeals Act.

The legislature also instructed THDA to confer with representatives of federal and state agencies, representatives from the home building and construction industry, and local government officials. The findings of this study are to be submitted to the General Assembly no later than February 1, 1999.

Findings from this study are presented in this report which attempts to examine a variety of affordable housing initiatives and program types throughout the country. The focus of the study is consistent with the specific requests for information contained within the House Joint Resolution.

Focus of the Study and Organization of the Report

In response to HJR 505, THDA conducted a study focusing on initiatives used in other states for developing affordable housing. In addition to the information gathered directly from agencies in other states, the study is based on published secondary analyses, and THDA's analysis of data from the censuses and other reliable sources. However sound an initiative may seem to be, it may not gain acceptance unless the market will support it and unless political or judicial support is strong enough to overcome any active opposition. The following list of analytical questions, all derived from HJR 505, were used to guide this evaluation.

- <u>Growth and Housing Affordability in Tennessee:</u> What do we know about population growth and housing affordability in Tennessee that might generate the need for affordable housing initiatives?

- Classification and Description of Initiatives: What *categories* of affordable housing initiatives adopted by other states and local jurisdictions have encouraged affordable housing construction and enhanced affordable housing opportunities for low- and moderate-income families? What were the salient features of successful initiatives in each category? From the history of successful programs, are there any common political climates or judicial activism that might have facilitated consensus building and conflict resolution around affordable housing development? How do these programs compare in terms of volume of production, cost effectiveness, and beneficiaries?
- Demographic and Economic Environment: What common demographic, economic, and housing market trends preceded the implementation of successful initiatives outside Tennessee? If specific demographic and market trends and political climates seem to be catalysts, are these trends also visible in the demographic, economic, housing market trends, and political climate in Tennessee? What local initiatives have been taken recently by Tennessee urban communities experiencing rapid growth?
- Industry Support. How does the community of builders and Realtors perceive these programs, especially their feasibility and efficacy in sustaining affordability in growing housing markets in Tennessee?
- Conclusions. Based on the above, what specific policy and program initiatives are worth considering in Tennessee? What are their strengths and weaknesses?

As discussed in subsequent sections of this report, affordable housing initiatives are developed as a result of several identifiable demographic and market trends. One of those trends involve shortages of affordable housing related to rapid population growth. We will first look at the prevalence of this condition within Tennessee.

PART II. Population Growth and Housing Affordability in Tennessee

Background on Population Growth in Tennessee

Nationally, 26 percent of all households enumerated during the 1990 census had to spend over 30 percent of their incomes for housing, thereby exceeding the widely accepted threshold of housing affordability. Housing conditions in Tennessee seemed a bit better in 1990, since only 23 percent of the Tennessee households exceeded this threshold of 30 percent. Since then, the Tennessee population has grown much faster than most other states, ranking 13th in growth during 1992-97 among the 50 contiguous states and the District of Columbia. It ranked only 24th in growth during 1987-92.

Most of the Tennessee counties experiencing substantial population growth are in suburbs of metropolitan areas or are contiguous to an MSA (Metropolitan Statistical Area). For example, 11 of the 21 counties that grew over 15 percent during 1990-96 are either in the Nashville MSA or are contiguous to it. Three of the 21 are in the Knoxville MSA also.

The central counties in the four largest MSAs grew below the state average level -- Shelby, Davidson, and Hamilton grew only in the three to five percent range during the six-year period. This pattern of rapid suburban and exurban growth, and meager growth in the central locations of the MSAs, suggests an ongoing trend in residential movements towards the metropolitan outskirts by householders who used to live and work in the central locations. As in other fast-growing states, continued movements of population of this kind, in the long run, tend to give a doughnut-shaped growth of suburban population around the metropolitan centers, leaving behind a number of abandoned homes and impoverished neighborhoods in the central cities. In states that experienced rapid population growth, it seriously affected housing availability and affordability. These states tried various measures to encourage affordable home construction as part of their urban growth strategies. Before we examine these state initiatives and their usefulness in Tennessee, it is pertinent to obtain first a good assessment of housing affordability in Tennessee. What is the picture of affordability from 1990 census data? What has happened since then that would have influenced it?

Chart 1. Counties Exceeding 15% Growth During 1990-96

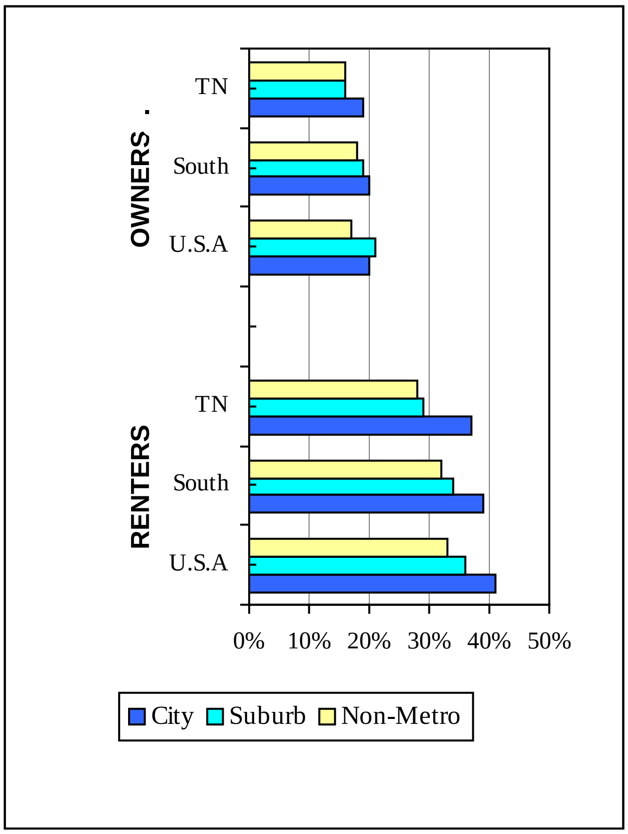
NASHVILLE AREA		KNOXVILLE AREA	
Williamson	31.0%	Sevier	20.2%
Rutherford	30.2%	Loudon	19.1%
Cheatham	22.2%	Blount	15.2%
Maury	21.7%		
Montgomery	20.3%	OTHER COUNTIES	
Robertson	19.7%	Jefferson	22.0%
Wilson	17.5%	Cumberland	21.1%
Marshall	16.9%	Tipton	19.8%
Stewart	16.1%	Johnson	19.8%
Hickman	16.0%	Wayne	17.0%
Sumner	15.9%	Meigs	15.6%
		Lake	16.9%

Source: Estimation of the Population of Counties: Annual Time Series, July 1, 1990 to July 1, 1996, Population Estimates Program, U.S. Bureau of the Census.

Basic facts about housing affordability in Tennessee in 1990:

- When compared to national and regional levels, Tennessee rental and homeownership markets are more affordable.
- The housing cost burden in rental markets is about twice that in ownership markets in Tennessee and elsewhere.
- Rental markets in central cities show the highest cost burden. Over 37 percent of Tennessee households renting in the metropolitan central cities experienced rent burdens in 1990.
- Younger and lower income households participate heavily in the rental market. A vast majority of households with rent burdens also have very low incomes. Rental subsidies play an important role in reducing their rent burdens.

Chart 2. Housing Cost Over 30% of Income



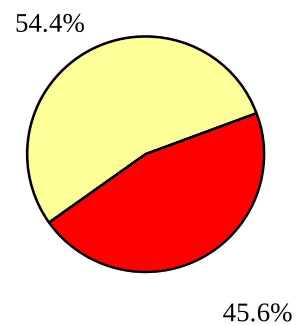
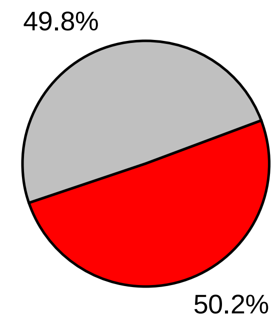
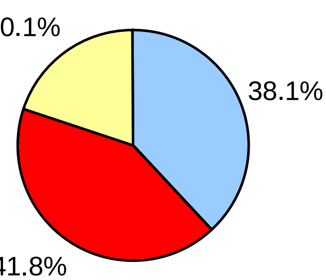
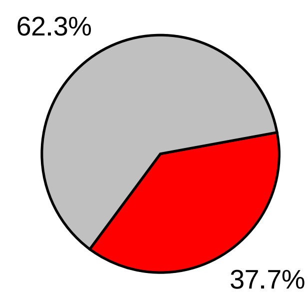
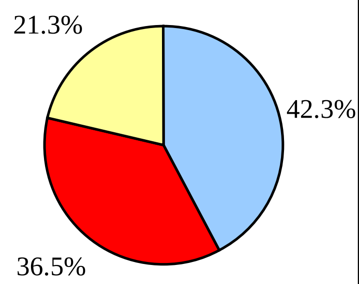
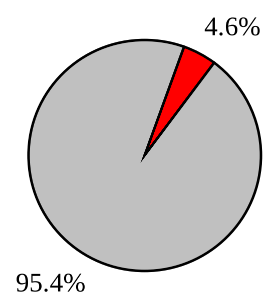
Source: THDA analysis of special CHAS tabulations of 1990 Census Data provided for HUD by U.S. Bureau of the Census.

Basic facts about affordability and availability in the Tennessee rental market:

- The lowest income group shown in Chart 3 is made of Tennessee households earning less than 30% of the area median. These households represent one-fourth of all Tennessee renter households. Almost an equal proportion of all occupied rental units, about 23 percent, are also affordable to this income group. Stiff competition for these very affordable units is evident from the fact that households in higher income brackets occupy 46 percent of these units. As a result, half of the lowest income renters live in units not affordable to them.

- Affordability is not as bad for renters in the 30-50% income group as only 38 percent of these households rent units not affordable to them. Even though they are only 16 percent of all renter households, their share of affordable units is 49 percent of the rental market and they occupy 20 percent of these affordable units.
- Almost all of the rental units in the local market (93%) are affordable to households earning 50-80% of the area median income; they form 21 percent of the renter households and occupy 21% of the affordable units in the market. Among these households, only five percent live in units not affordable to them.

Chart 3. Renter Occupancy

Income Group	% of All Renters	% of all units affordable	Who Rents These Units?	Do they live in affordable units?
Extremely Low (<30%)	24.6%	22.6%		
Very Low (30-50%)	15.7%	48.7%		
Low (50-80%)	20.7%	92.7%		

Lower Income
Higher Income
This Group

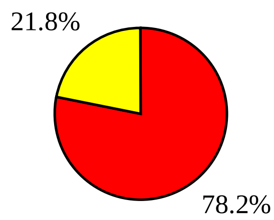
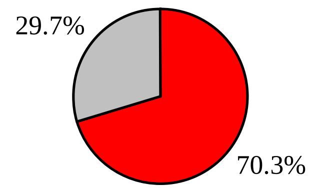
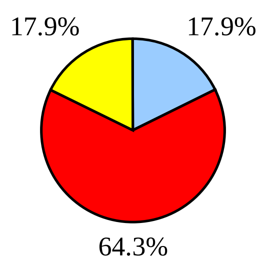
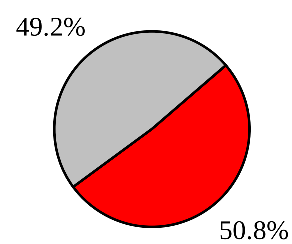
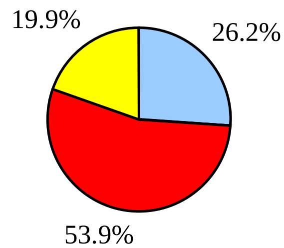
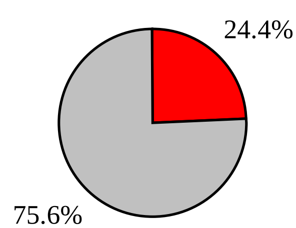
No Yes

Source: THDA analysis of special CHAS tabulations of 1990 Census Data provided for HUD by U.S. Bureau of the Census.

Basic facts about affordability and availability in the Tennessee homeowner market:

- The lowest income group of owners in Tennessee form less than nine percent of all homeowners in 1990. About 12 percent of all owner occupied units are also affordable to this income group. Stiff competition for these very affordable homes is also evident from the fact that households in higher income brackets occupy 78 percent of these units. As a result, 70 percent of the lowest income owners live in units not affordable to them.
- Almost half of the owners in the 30-50% income group live in homes not affordable to them. Even though they are only 10 percent of all owner households, their share of affordable units is only 27 percent of the owner market and they occupy 18 percent of these affordable units.
- More than half (57%) of the owner units in the local market are affordable to owner households earning 50-80% of area median income. They form 15 percent of all owner households and occupy 20 percent of the affordable units in the market. One-fourth of them live in homes not affordable to their income bracket.

Chart 4. Owner Occupancy

Income Group	% of all Homeowners	% of all units affordable	Who Owns These Units?	Do They Live in Affordable Units?
Extremely Low (<30%)	8.7%	11.9%		
Very Low (30-50%)	9.6%	26.4%		
Low (50-80%)	14.8%	56.5%		

Lower Income
Higher Income
This Group

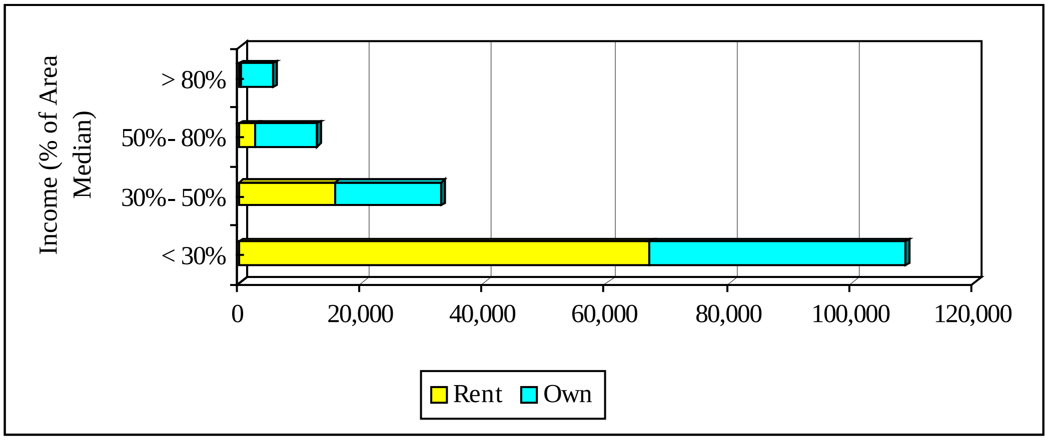
No Yes

Source: THDA analysis of special CHAS tabulations of 1990 Census Data provided for HUD by U.S. Bureau of the Census.

Severity of housing cost burden in Tennessee

There were about 160,000 Tennessee households in 1990 who spent over 50 percent of their incomes for housing; 109,000 of them, as the chart below shows, earned less than 30 percent of the area median income. These households could easily become homeless.

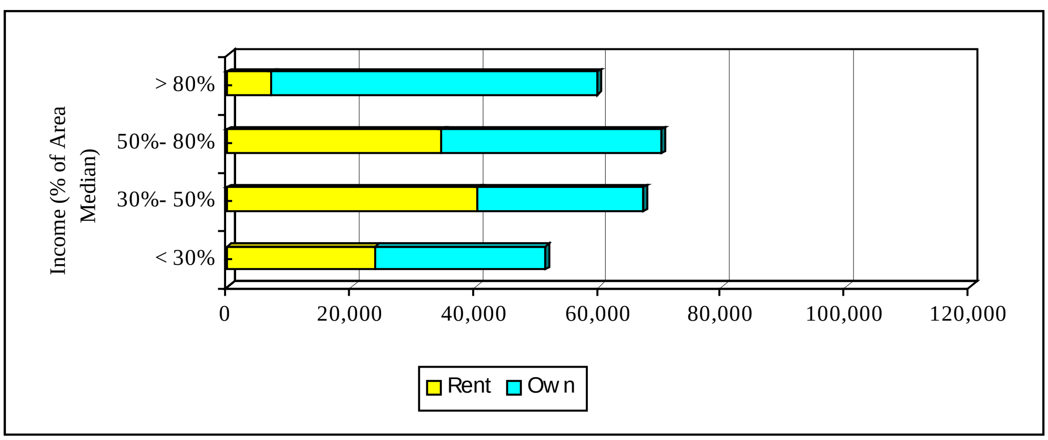
Chart 5. Number of Households with Housing Cost >50% of Income



Source: THDA analysis of special CHAS tabulations of 1990 Census Data provided for HUD by U.S. Bureau of the Census.

Burdened also, but not as severely as the above households, were 248,000 Tennessee households who spent 30 to 50 percent of their incomes for housing. They came from all income strata. The highest income category of these households consists predominantly of homeowners.

Chart 6. Number of Households with Housing Cost 30-50% of Income



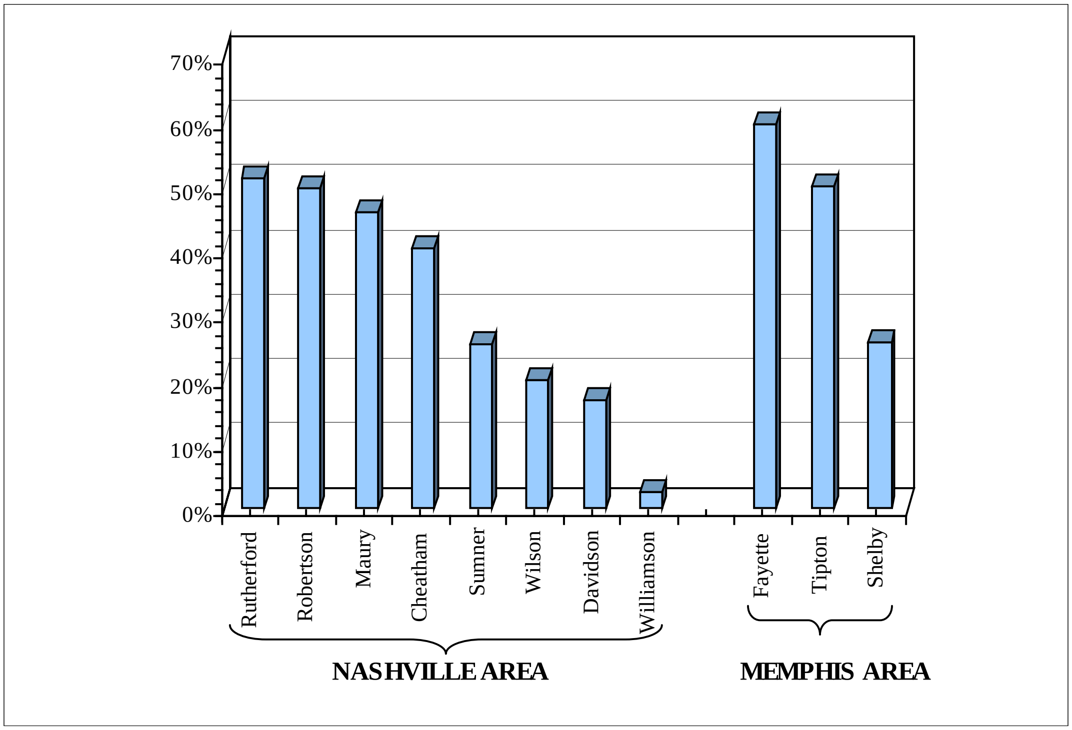
Source: THDA analysis of special CHAS tabulations of 1990 Census Data provided for HUD by U.S. Bureau of the Census.

Homeownership Affordability in Tennessee Metropolitan Areas

Almost all (98%) of the new homes sold in Williamson County in 1996 exceeded the price of $100,000. Also, very few new homes were sold below this price in Davidson, Sumner, and Wilson

Counties. However, news homes sold at prices below $100,000 were not as rare in other Nashville area counties or in Memphis MSA counties, other than Shelby.

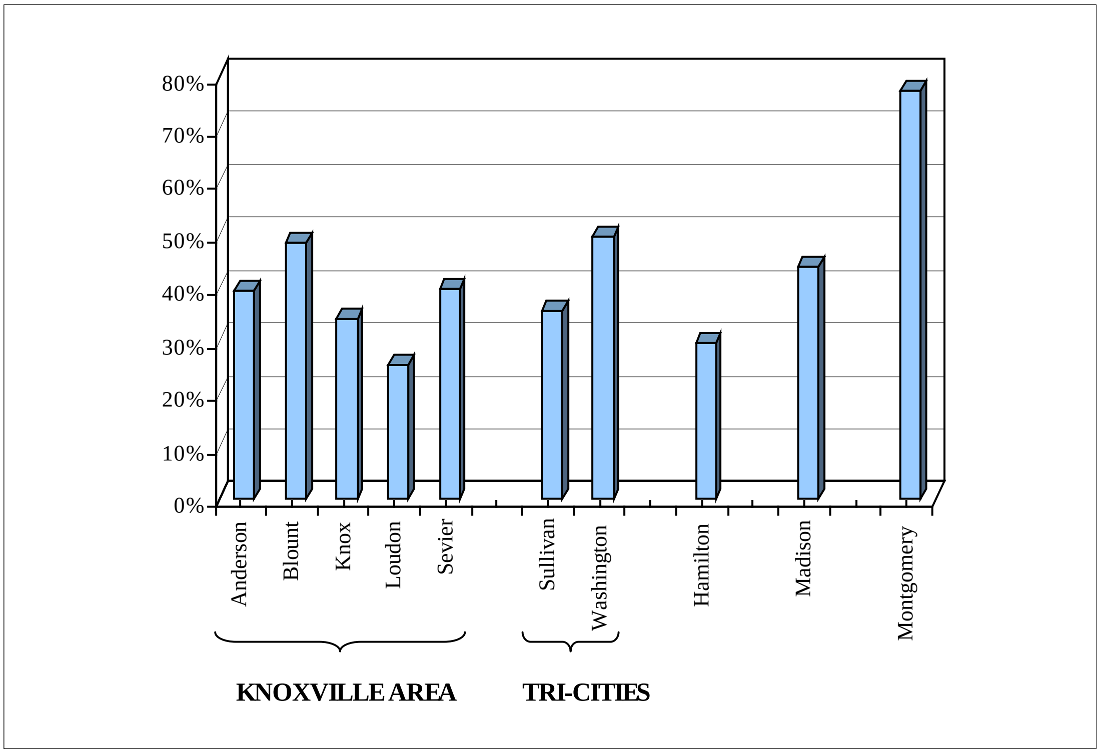
Chart 7. Percent of New Homes Sold below $100,000 in 1996



Source: THDA analysis of 1996 Home Sales Price data maintained by the Property Assessment Division, Comptroller's Office, State of Tennessee.

Loudon County in the Knoxville MSA resembles Sumner and Wilson Counties in new home sales prices. In all the other MSA counties, over 40 percent of the new homes sold in 1996 were priced below $100,000. Lack of affordable new homes is reflected mostly in the Nashville MSA, primarily in Williamson County.

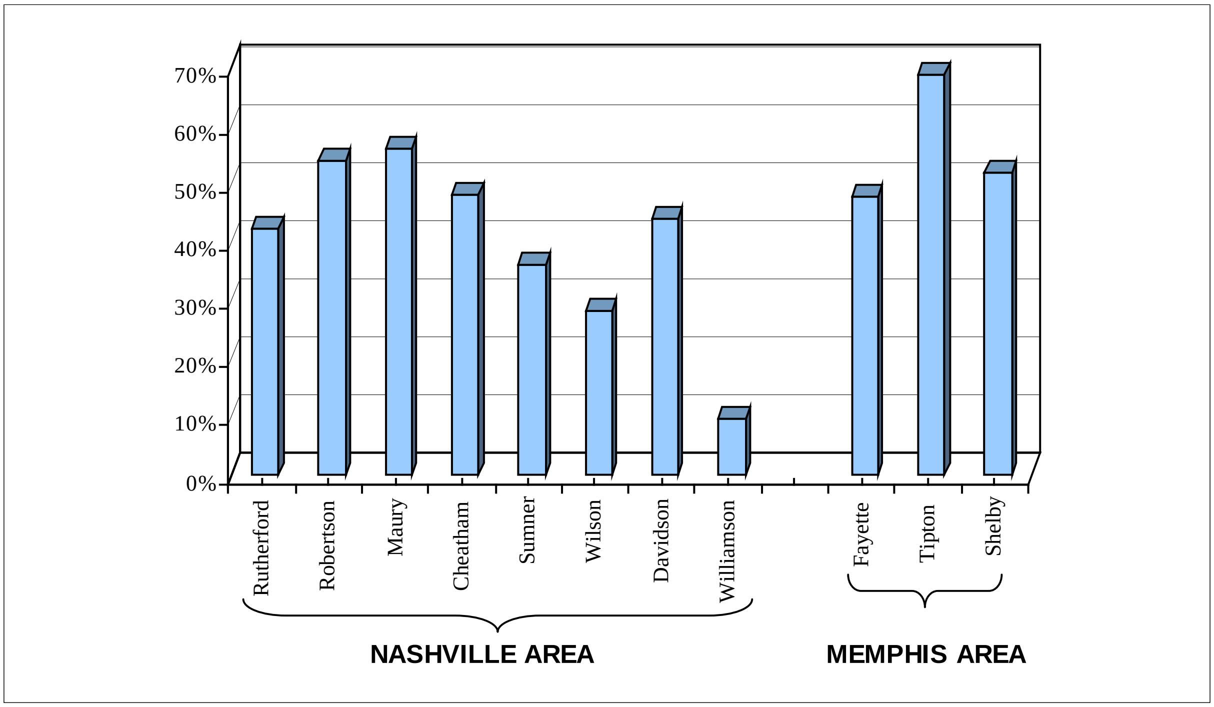
Chart 8. Percent of New Homes Sold below $100,000 in 1996



Source: THDA analysis of 1996 Home Sales Price data maintained by the Property Assessment Division, Comptroller's Office, State of Tennessee.

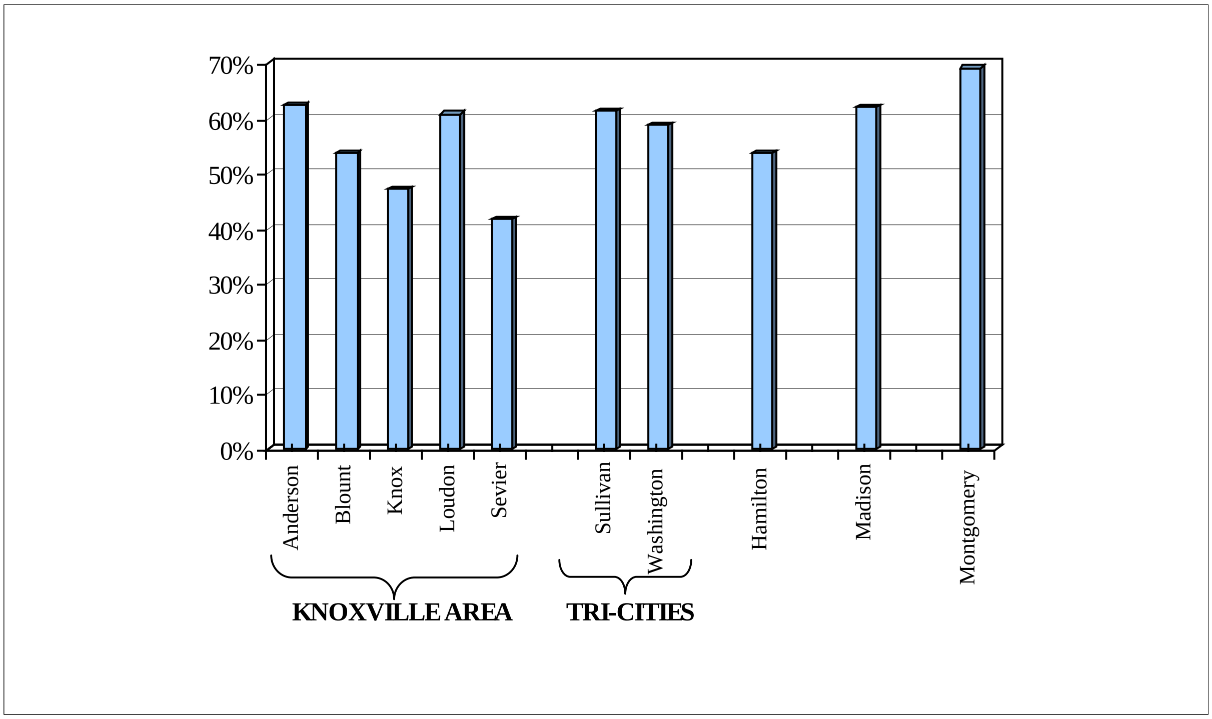
If existing homes below $85,000 in price are considered affordable, a significant portion (exceeding 40 percent in most cases) of the existing homes sold in 1996 in metropolitan counties in Tennessee fit this description. Williamson County is the major exception, where less than 10 percent of the existing home sales met this definition. These findings lead to a conclusion that concerns about the availability of homes for sale at reasonable prices are relevant in Williamson County and, to a lesser extent, in Davidson, Sumner, and Wilson Counties.

Chart 9. Percent of Existing Homes Sold below $85,000 in 1996



Source: THDA analysis of 1996 Home Sales Price data maintained by the Property Assessment Division, Comptroller's Office, State of Tennessee.

Chart 10. Percent of Existing Homes Sold below $85,000 in 1996



Source: THDA analysis of 1996 Home Sales Price data maintained by the Property Assessment Division, Comptroller's Office, State of Tennessee.

PART III. Affordable Housing Initiatives and Program Models

Background

The historical experience of other states which have undergone rapid population growth during earlier decades may offer some insight on what consequences growth may have on housing affordability in Tennessee. We will look at the demographic and economic pressures accompanying growth in other parts of the country that resulted in government support of initiatives for affordable home construction.

Housing markets usually faced problems that required corrective public intervention (a) when homes priced reasonably low became unavailable for purchase or for rent, and/or (b) when families who could least afford the market housing prices resided or sought residence in the area. Public remedy was also sought when historical patterns of growth and migration led to enclaves of low-income residents, often in central locations of metropolitan areas. These lower income residents also faced barriers to moving out of the central city because of exclusionary zoning ordinances and expensive subdivision requirements in the suburbs.

Types of Initiatives to Produce Affordable Housing

The shortage of affordable housing has resulted in affordable housing initiatives and programs in some areas. In this study, we have reviewed a number of these initiatives and programs. In some cases, in-depth analyses are provided, especially when the programs seem pertinent to the state of Tennessee. In other cases we have simply provided information on the program type and examples of each in areas throughout the United States.

<u>Inclusionary Zoning and Density Bonus Programs</u>

One of the most important affordable housing incentives, and one that was specifically mentioned in HJR 505, is inclusionary zoning and density bonus ordinances. Any discussion about models for inclusionary zoning and density bonus requires at least some brief description of the two types of programs before understanding their possible application to the State of Tennessee. Below are brief facts about inclusionary zoning as provided by Peter Werwath, Senior Program Director, of the Research, Evaluation and Documentation Division, for the Enterprise Foundation.[1]

- <u>Inclusionary zoning</u> generally refers to local ordinances or guidelines that require or encourage residential developments to include a certain percentage of affordable housing. (However, some states have adopted legislation that enables or clarifies the local governments' rights to adopt these ordinances.)
- Most of these types of programs are aimed at assisting families with incomes at 80 percent or 100 percent of median income, rather than the neediest households.
- Inclusionary housing may be on or off site. That is, affordable housing may be "included" with more expensive development, or built at a separate site within the same general vicinity.
- Often payments may be made to a trust fund in lieu of providing affordable housing.
- Inclusionary zoning programs may be either voluntary or mandatory.
- Inclusionary zoning must have a reason i.e., it must have data and an argument that proves an historical relationship between the construction of higher priced housing and commercial

properties and the lack of affordable housing, and the economic and social ills that have resulted from it.

Inclusionary zoning must have a definition of affordable housing and must include a firm definition of what developers must deliver and to whom.

Density bonus programs allow builders to increase the number of units in a property based on fulfillment of specified zoning requirements. Increased density might be allowed for any of the following reasons:

- Inclusion of a specified percentage of low-income or affordable housing units;
- Dollars contributed to the city or county for road work or infrastructure;
- Land donated by the developer to build a school or other public facility.

Examples of Inclusionary Zoning and Density Bonus Programs

Perhaps one of the most notable and successful inclusionary housing programs in the country can be found in Montgomery County, Maryland. Another program, located in Fairfax County, Virginia, has achieved some success in inclusionary zoning using density bonuses, but differs from the Maryland program. A description of each follows:

Example 1: Montgomery County, Maryland

Montgomery County, Maryland is located immediately to the north of Washington, DC, and is the most populous county in Maryland with a 1996 population of approximately 819,000. In the early 1970's (and for several decades prior), the county experienced rapid population growth and began to experience a shortage of housing affordable to low and moderate-income households.

Adopted in 1974, the Montgomery County, Maryland, inclusionary zoning program is a part of the local Moderately Priced Dwelling Unit (MPDU) ordinance. Originally, the County Executive vetoed the legislation because he believed it to be unconstitutional, invasive public policy, and too difficult to administer. However, the County Council subsequently overrode the veto and the law went into effect. According to the County's Department of Housing and Community Affairs, the MPDU program is "believed to be the country's first mandatory, inclusionary zoning law that specified a density bonus allowance to builders for providing affordable housing."[2] Specifically, the ordinance requires developments of 50 or more units to include 12.5 percent of MPDUs. The law applies only to property zoned one-half acre or smaller. A portion of the MPDUs (up to 40%) can be purchased by the local housing commission or local non-profits for use in affordable rental programs. Households having an income at or below approximately 65 percent of the area's median income, adjusted for family size, qualify for the program, with priority given to those who work or already live in the county.

To make the program work, Montgomery County provides a density bonus to developers. Within local planning constraints, a builder is granted the ability to build up to 22 percent more units in the subdivision than otherwise would be allowed. Density bonuses are granted on a sliding scale as the percent of affordable units increases, up to the maximum bonus of 22 percent. No density bonus is granted for the minimum set-aside of 12.5 percent. The density bonus, in effect, creates free lots upon which the MPDUs are constructed. It is important to note that this program has produced nearly 10,000 affordable units since 1974.

The program was administered in the County's Department of Housing and Community Development, and had an operating budget of approximately $350,000 (in 1996). The price for which the unit can be resold is controlled for 10 years and any "windfall" profit from the first sale of the unit must be split between the County and owner. Rental units have rent controls for a period of 20 years. The county states that "although, in the past, builders expressed objection to some of the procedures and regulations, they are generally supportive of the program and have made numerous suggestions for its improvement." (DHCA program description, 1996) County materials also note that the most significant limitation of the program is its reliance on a favorable housing market -- the production of MPDUs is dependent on the production of market rate housing.

Example 2: Fairfax County, Virginia

Located to the west, southwest of Washington, DC, Fairfax County shares many economic and demographic features with Montgomery County, Maryland. Indeed, many of the factors which contributed to Montgomery County's decision to adopt inclusionary zoning and density bonuses also contributed to the decision in Fairfax County, Virginia, to adopt a program modeled after the Maryland program. Fairfax County originally tried to adopt such a program in the early 1970's, but it was struck down by the Virginia Supreme Court. Subsequent legislation was not passed until 1990, after the state had passed legislation specifically allowing the county to pass such legislation.

The Fairfax County, Virginia, Density Bonus Ordinance program is a part of its Affordable Dwelling Unit (ADU) ordinance. A key distinction of the Fairfax County program from the Montgomery County program is that participation in the Virginia program is **not mandatory** on the part of the developer. However, the legislation does impose mandatory requirements on developers who choose to participate. State legislation also imposes mandatory requirements on localities that choose to provide an affordable dwelling unit program. The purpose of the incentives offered by the program is to encourage developers to participate in the program.

The Fairfax County ordinance applies to residential developments which are subject to rezoning, special exception, site plan, or subdivision plat approval in the following situations: 1) the site is to be developed at a density greater than one dwelling unit per acre; 2) the site has 50 units or more; and 3) the site is located within an approved sewer service area. Developments are allowed a 20 percent increase in density in exchange for the mandatory 12.5 percent set-aside for affordable single-family attached or detached housing. Also in contrast to the Maryland program, this is a set ratio, there is no sliding scale. This ratio is more generous to the developer than the Maryland ordinance. With its sliding scale, Montgomery County developers would have to make a 14.5 percent set-aside to get a 20 percent bonus (as compared to 12.5% in Fairfax County); these developers would get no density bonus for providing the minimum required set-aside of 12.5 percent. Fairfax County says that this ratio was negotiated with developers and community interest groups who concluded that the 12.5 percent set-aside was the right amount to assure that developers experienced "no economic loss."[3] In the first three years of the program, 27 affordable housing units were sold, 27 more were under construction, and 334 had been approved for construction as set-aside units. It is important to keep in mind that, by the time this program was adopted, the remarkable growth in housing that had been experienced twenty years earlier (when Montgomery County's program was adopted) had slowed very considerably.

Example 3: Programs in the State of California

In California, inclusionary housing programs have become a significant element in the provision of affordable housing statewide. Heavy in-migration beginning in the 1970's and the inability of the housing industry to keep up with demand, accompanied by growth control and other land use planning regulations contributed to a crisis in housing affordability in California.

Since 1975, the California General Plan Law has required that municipalities have a five-year plan that "shall make adequate provision for the existing and projected needs of all segments of the community" and identify potential housing sites "for all income levels." The law was amended in 1980 to require each locality to create policies and programs to enable it to meet its "fair share" of regional lower-income household needs.

In 1989, a state density bonus law was created to offer a land use-based option to facilitate the economic feasibility of affordable housing development. The 1989 law provides that local governments shall grant either a density bonus of at least 25%, or a density bonus with additional incentive(s), or equivalent financial incentives to housing developers who agree to provide 1) at least 20% of the total units of the housing development as target units affordable to lower-income households; or 2) at least 10% of the total units to very low-income households; or 3) senior citizen housing. As of 1997, all California inclusionary housing programs offered some type of cost offsets to developers in the form of financial assistance and/or regulatory relief in an attempt to counter the costs incurred in providing affordable units.

The results of a 1994 survey by the State of California found that 64 jurisdictions had adopted inclusionary housing programs that had produced a total of 22,572 units, with an additional 2,439 units in the approval process. Sixty-six percent of the programs were mandatory. The typical minimum project size was 10 units, and the majority of the programs required 10 to 15 percent of new residential development projects be affordable. Sixty-one percent permitted the developer to pay a fee in lieu of providing affordable housing while others permitted an in-lieu donation of land.

Over the years, the effectiveness of inclusionary housing programs in California have been influenced by a changing political climate and as seen in Montgomery County, Maryland, shifts in the economy that have affected local building activity.[4]

Some General Conclusions About Inclusionary Housing Programs

- Inclusionary housing has generally been a local initiative. Its success or failure depends mainly on local conditions -- political, economic, housing market and demographic.
- In order to adapt the program to local conditions, inclusionary housing models allow a variety of choices regarding incentives, requirements, and alternate developer options. The diversity of inclusionary housing programs in California exemplifies this.
- It is this flexibility that has kept inclusionary housing popular for over 30 years.
- States have played a pivotal role by encouraging localities to consider affordable housing initiatives and by enabling local governments to adopt necessary ordinances. In California, the Housing General Plan Law and the state-mandated fair share doctrine gave significant impetus for local enactment of inclusionary housing programs.
- Maintaining the affordability of inclusionary housing program units has been a major problem, even though a majority of the programs require that affordability provisions are observed for 30 years.

- Inclusionary housing programs often allow in-lieu fees, off-site units, and fewer amenities. These cost offsets to developers reduce the potential of fostering economic and racial residential integration through the program.

Possible Applicability of Inclusionary Zoning and Density Bonus Programs

In examining the programs above, we considered Williamson County, Tennessee to be a location with many of the same demographic and economic characteristics. Below we compare the Williamson County Density Bonus program to those of Montgomery County, Maryland, and Fairfax County, Virginia.

Some observations on the applicability of inclusionary zoning and density bonuses:

- The Montgomery County MPDU ordinance continues to be a viable mandated prescription for affordable housing construction. It has consistently produced moderate numbers of affordable units during the past 25 years. As the ordinance mandates, the production of affordable housing is dependent on the overall new construction volume.
- The more recent Fairfax County ordinance, lacking any mandatory ties to overall production, has produced fewer affordable units. It also faced critical review and substantial revision recently. As a result, it has changed to have many of the provisions in the Montgomery County ordinance. For example, sales-price and rent control periods of 10 and 20 years, respectively, and a sliding scale for density bonuses have been added.[5] These Fairfax County actions reinforce the notion that Montgomery County gives one of the best working models for any inclusionary program.

Programs in Williamson County, Tennessee

Williamson County has been faced with the challenging task of integrating affordable housing development concurrently with its rapid economic development. The 1997 report of the Greater Nashville Regional Council describes this challenge this way:

> *The tremendous commercial growth in Williamson County had created a need for expanding the workforce. With unemployment rate of well under 3% the availability of a good labor force is critical to sustained growth. The Franklin/Williamson County Chamber of Commerce is actively working to resolve this problem by seeking ways to increase affordable housing in the area and finding transportation for workers from surrounding counties.*

Williamson County passed a housing bonus ordinance in 1988. The ordinance "provides an incentive for the development of affordable housing within the county in the Suburban and Urban districts" by allowing greater densities when housing for moderate-income households is included in a development. The ordinance was designed to,

> ...provide additional housing opportunities for low-income persons and for those with more moderate-incomes who are being forced out of the housing market in Williamson County by inflationary pressures.[6]

To date, the Williamson County density bonus ordinance has failed to produce a significant number of affordable housing units. This is probably, at least partially, because population density in Williamson County has not reached a problematic level (see Chart 14) and because the provisions of the ordinance are not mandatory.

The following chart provides information specific to the four out-of-state inclusionary housing and density bonus programs discussed in the preceding chapter.

Program Description

County and State	Montgomery County, MD	Fairfax County, VA	California	California
Program/Ordinance name	Moderately Priced Dwelling Unit (MPDU) ordinance; Adopted in 1974	Affordable Dwelling Unit (ADU) ordinance; Adopted in 1990.	California General Plan Law; Adopted in 1975 and amended in 1980.	Residential Density Bonus ordinance; Adopted in 1989.
Program type	Mandatory inclusionary zoning law with a density bonus allowance.	Voluntary inclusionary zoning law with a density bonus allowance.	Mandatory comprehensive housing element for all municipal and county governments. A legislative act that fostered inclusionary programs.	Mandatory density bonus and/or financial incentive law for local governments.
Program description	Requires developments of 50 or more units to include 12.5% of MPDU's. Density bonuses are granted on a sliding scale as the percent of affordable units increase. No bonus is granted for the minimum set aside of 12.5%.	A site of 50 or more units developed at a density > 1 unit per acre and is located in an approved sewer service area qualifies for a 20% increase in density in exchange for a mandatory 12.5% set aside for affordable single-family units10% density increase	Requires municipalities have a 5-year plan that shall identify potential housing sites "for all income levels"; Amendment requires each locality to create programs to enable it to meet its "fair share" of regional lower-income household needs.	Local governments shall grant a density bonus of at least 25% and/or additional incentivest to developers who agree to make (1) at least 20% of the total units affordable to lower-income households; or (2) at least 10% to very low-income households; or
Goal	To produce moderately priced housing for County residents and workers; to distribute low & moderate income households throughout county growth areas.	Develop affordable housing units through new construction with mixed income environment..	To motivate local governments to meet their housing responsibilities.	To develop affordable housing.
General description of incentives	A builder is granted the ability to build up to 22% more units in the development than otherwise would be allowed.	The purpose of the density bonus offered by this program is to encourage developers to participate in the program.	Preference in the allocation of housing and community development funds is given to those jurisdictions that are in compliance with the law.	Makes it possible for inclusionary housing programs to offer cost offsets to developers in an attemp to counter the costs incurred in providing inclusionary units.
Recipients of incentives	For-profit developers	For-profit developers	For-profit developers	For-profit developers
Variations in incentives and priority	Up to 40% of MPDU's can be purchased by the local housing commission or local non-profits for use in affordable housing programs. Priority is given to households who work or already live in the county. The MPDU requirement falls within a range of 12.5% to 15% based on actual bonus density achieved.	Gives real estate agents a 1.5% commission for selling low-income units; allows builders to construct 90% of a development before they have to build 90% of its ADUs; makes it possible for the county's housing authority to purchase 1/3 of for-sale units or lease 1/3 of rental units to use as publis housing.	There is considerable variation in the programs. However, about 90% of them are mandatory and nearly 2/3 of them require an inclusion typically from 10 to 15% of the market rate units. Two-thirds of them allow payment of a fee in lieu of providing affordable units and 62% don't require affordable units to be provided on-site.	Most of the incentives are in the form of density bonuses. Others include fee waivers, fast-track permit approval, relaxation of design restrictions and low-cost financing from community block grants and state housing finance agency sources.
Affordability requirements: price&location	The resale price for an affordable unit is controlled for 10 years and any "windfall" profit from the sale must be split between the county and owner. Rental units have rent controls for a period of 20 years.	In 1998, reduced the length of price cintrols on for-sale ADU units from 50 to 15 years and on rental units, from 50 to 20 years.	The period of required affordablitiy ranges from 5 years to perpetuity.	Varies amongst the jurisdictions. Same as under the General Plan.
Affordability requirements: Beneficiary	Households having an income at or below approximately 65% of the area's median Income qualify for the program.	Household income must be <=70% of Wasington, DC MSA area median to qualify. In multi-family projects, 1/3 of units are leased to households with incomes <= 50% of MSA median if subsidies are available.	Housing need is specified by four income levels: < 50% area median; 50-80%; 80-120%; and above 120% of area median. Some areas distinguish a separate range of < 30% of area median.	Same as under the General Plan.
Funding Source/Enforcement	Administration and enforcement of the program takes place in the County's Dept. of Housing & Community Development. It has an operating budget of approximately $350,000 (1996).	Administered by the Department of Housing and Community Development.		State Department of Housing and Community Development (DHCD) reviews housing elements for compliance.

Production Statistics	9,511 units (through 1995)	500 units since program inception.	20,000 units (through 1992)
Beneficiary Profile	Approximately 70% owner occupied; 30% rental. Housing authority or non-profits operate about 1,000 of the units, typically with subsidies for very-low-income occupancy	Only 15 units owned by the housing authority for rent (with subsidies) to lower income households.	Varies amongst jurisdictions. Orange County produced about 1/3 of the statewide total.
Notes		*Recently changed to a sliding scale that links the number of affordable units required to the amount of bonus density.	

Other Types of Housing Programs

As part of research for this study, HJR 505 specified that we look at affordable housing programs specifically being run or undertaken by Housing Finance Agencies (HFAs) throughout the country. THDA designed a survey and sent it to all Housing Finance Agencies in the United States, as well as the District of Columbia and the US Virgin Islands. Results from this survey provided information on affordable housing initiatives not discussed in preceding sections of this report. These include construction loan programs, tax abatement programs, and other unique programs. Summaries are provided below.

Construction Loan Programs

According to the results of our survey, one of the most popular types of state-administered programs to encourage development of affordable housing is variety of construction loan programs. These programs provide construction financing for developers at below-market interest rates, sometimes with other incentives. Responses from at least seven states indicated that their state sponsored such a program. Below, we describe those that seem best suited for consideration in Tennessee.

Mississippi's Affordable Housing Development Fund was established to "finance the construction and purchase of new owner-occupied housing meeting the purchase price limits of the Mortgage Revenue Bond Program and to finance the construction of rental housing meeting the requirements of the Low Income Housing Tax Credit Program." It provides construction loans for new owner-occupied or rental housing with interest rates "as low as 3.00%." Although termed a construction loan program, the loans have terms of up to 20 years, with 10 or 15 year terms for loans to corporate or other for-profit borrowers (depending on whether the development is in a targeted area or not). The program gives priority to housing for households earning up to 115 percent of county median income and to financing of ten years or less. Size of available loans is dependent upon several criteria; the loan fund can contribute up to 33% of the project financing. This fund was originally capitalized at $2 million by the Mississippi Legislature in 1993; an additional $6 million was authorized in the 1994 session, and $5 million was authorized in the 1998 session. Program statistics show that the program has primarily been used to finance rental housing and, instead of short-term loans for the period of construction, developers have used long-term loans. The program has been successful in funding the development of over 600 affordable housing units.

The Kentucky Housing Development Fund (HDF) is a short-term construction loan pool. Kentucky requires local lender(s) to participate in development loans. In addition, a percentage of homes developed must be set aside for Kentucky Housing Corporation (KHC) income eligible home buyers, to be sold at a purchase price not greater than $86,000. The proportion set aside for "affordable" homes must be in the same percentage as KHC participation in the development loan. Typical loan terms range from six to 24 months, with the principal on most construction loans being paid upon sale of the unit(s). This much shorter loan term and the fact that the program is used more for homeowner-occupied units appear to be the primary differences between this program and that of Mississippi. Interest rates depend upon current market conditions, but are currently at 5% for for-profit builders and 3% for nonprofits. Homebuyers, as long as they are KHC-income eligible, may secure financing from KHC or other permanent loan program of their choice. By state statute, KHC is authorized to issue housing development fund notes to fund the HDF, with a limit that not more than $5 million in fund notes or other borrowings shall be outstanding at any one time. Program statistics indicate that a total of more than 2,000 affordable housing units have been created by this program.

The New Hampshire Affordable Housing Fund was established to "facilitate the purchase and rehabilitation or construction of affordable housing primarily for low and moderate-income persons and their families, and for pre-construction technical assistance." The Housing Finance Authority (HFA) may disburse the funds as either grants or loans to both for-profit and nonprofit organizations. Projects receiving financial assistance shall have at least 50% of their units affordable to persons of low or moderate-income (not defined more specifically in the statute). There also has to be a finding that there exists a shortage of good housing for persons in these income groups within the "general housing market area" proposed for the project. Both long-term mortgage loans to finance the total cost of the project and short-term loans to supplement the use of other funds are available. Program statistics show that this program has been used almost exclusively for multifamily rental housing and that it has successfully created over 600 units of affordable housing since its inception.

The South Carolina Housing Trust Fund provides financial assistance for development of affordable housing for lower income and very low-income households. Trust Fund awards may be used to finance owner occupied housing, multifamily rental units or group homes. All awards made by the Fund are in the form of loans which may be forgiven if the property is used in accordance with the terms of the funding agreement for at least 20 years. Funding for the program was provided by an increase in the state stamp tax of 20 cents per $500 of real estate sold, which usually generates about $2 million per year.

The New Jersey Urban Home Ownership Recovery Program (UHORP) provides construction financing for developers of mixed income urban for-sale homes, targeting urban centers. Both for-profit and non-profit entities are eligible to apply. Projects must be comprised of 10 or more homeownership units. Low and moderate-income projects are eligible to apply; however, all projects are encouraged to include a market mix. Projects designed for the occupancy of predominantly (more than 50%) low-income residents will not be considered. UHORP consists of three distinct components.

Construction financing: The Agency will loan up to 50% of the amount required to complete the project. A co-first lead lender will lend the matching 50% to make up the balance of the loan. The lender underwrites the loan and development budgets; approves plans and specifications; makes progress inspections; approves draw requests and disburses Housing Incentive Funds (HIF) and UHORP funds. The Agency establishes a floating interest rate approximately two hundred basis points below the interest rate offered by the lead lender. Therefore, the borrowed funds will be at the blended Agency/lender rate.

Housing Incentive Fund: This fund provides funds, in the form of a grant, to construct low and moderate income units in eligible mixed income projects. There is a maximum amount of $25,000 for moderate-income units or market units built and $45,000 for low-income units. The maximum assistance on a two-family dwelling is $50,000. Developers requesting HIF funds must utilize the construction loan component of the program.

Permanent End Loan Financing: This component of the program is optional. Eligible first time and urban homebuyers may apply for loans through the Agency’s Home Buyers Program administered through a network of participating lenders. Developers may also request approval to participate in this 100% financing program.

Various other states have programs designed to defray construction financing costs for development of affordable housing, but usually with more targeted purposes than those cited above. Pennsylvania’s Penn HOMES project is designed to assist in the development of multifamily housing for very low income people (all units restricted to persons with income no greater than 60 percent of median) through low-interest deferred loans. Oregon has a Housing Trust Fund which provides grant funds for the development of affordable housing, with the amount of funds available based on the proportion of the project to be dedicated to low or very low income units (the Oregon Legislature set aside $14 million to create this fund in 1991).

Construction loan programs offer several benefits. They provide a direct cost incentive to developers of housing, both affordable and mixed income. They are less costly for the administering entity in the short term than tax abatement programs because, in most of the examples given, the funds are provided in the form of a loan. However, the costs of administering the programs are probably higher than tax abatement programs over a longer period of time, because of having to service the loans for their duration. From a developer’s perspective, the lower financing costs would need to approach the additional profit made by developing more expensive housing in order for this incentive to produce significant new affordable housing.

The following chart contains specific information on a variety of construction loan programs throughout the country.

AFFORDABLE HOUSING INITIATIVES: CONSTRUCTION LOAN PROGRAMS

Program Description

State	Mississippi	Kentucky	New Hampshire	South Carolina	New Jersey
Program name	Affordable Housing Development Fund (MAHDF); created 1992	Housing Development Fund (HDF) administered by Kentucky Housing Corporation (KHC); created 1974	Affordable Housing Fund; created 1988	Housing Trust Fund; created 1992	Urban Home Ownership Recovery Program (UHORP); started 1996
Program type	Construction Loans-Long Term; Also DPA loans to individuals	Construction Loans- Short Term	Construction & Acquisition/Rehab Loans	Construction Loans	3 Components: Construction Financing; Housing Incentive Fund; Permanent End Loan Financing.
Program description	Finance the construction and purchase of new affordable homes and the construction of affordable rental housing.	Finance new development of homes with a percentage set aside for KHC income-eligible buyers at a purchase price of $86,000 or below.	Facilitate the purchase and rehabilitation or construction of affordable housing primarily for the low and moderate income.	Finance the development of affordable housing (Single family homes, multifamily rental units or group homes) for low income and very- low income households.	Construction financing at below-market rates; all units for homeownership; primarily single-family homes with limited availability for two-family homes; HIF also provides for grant funding to supplement loans in certain instances.
Goal	Develop affordable housing	Develop affordable homes	Develop affordable housing	Development of affordable housing	To encourage the development of mixed income housing in urban areas & to assist with revitalization of neighborhoods.
General description of incentives	Low-interest construction loans (interest as low as 3%) for up to 20 years; loan fund can contribute up to 1/3 of project financing.	Short-term construction loans (usually 6 to 24 months). Interest rates are below-market and vary over time. Currently 3% for non-profits and 5% for others. Principal on most of these loans paid upon sale. Developers required to have local lender participation.	Long-term mortgage loans to finance the total cost of the project and short-term loans to supplement the use of other available funds.	All awards made by the fund are in the form of loans which may be forgiven if the property is used in accordance with the terms of the funding agreement for at least 20 years.	Agency loans up to 50% of project funds; floating interest rate approx. 200 basis pts. below private lender rate; private (lead) lender provides admin. and servicing duties. Projects must have at least 10 units.
Recipients of incentives	For-profit and non-profit developers	For-profit and non-profit developers	For-profit and non-profit developers	For-profit and non-profit sponsors	For-profit and non-profit developers

AFFORDABLE HOUSING INITIATIVES: CONSTRUCTION LOAN PROGRAMS

State	Mississippi	Kentucky	New Hampshire	South Carolina	New Jersey
Variations in incentives and priority	For-profits can get up to 15-year terms in targeted areas, otherwise up to 10 years. Priority given to beneficiaries below 115 % of county median income and to financing of ten years or less.	In addition to loans to developers, this fund provides downpayment and closing costs assistance, and makes interest payments for persons of low and moderate income.	Almost exclusively used for multi-family housing; priority given to projects with (1) highest # of units affordable to low income persons (2) longest commitment to low income persons (3) limited equity coops in which membership is mostly low or moderate	Used mostly for group homes for the disabled and multifamily rental units. Provide 50% of financing for group homes or cap the loan amount at $60k. Currently, 2% interest rate for multifamily project loans considered hard debt.	Projects must be located in certain urban municipalities; reasonable per sq. foot cost standards; minimum size standards; max. developer fees; Projects with at least 30% market units receive highest priority; Projects with >50% low-income units not considered.
Affordability requirements: price & location	MRB price limits for home construction and LIHTC requirements for rental construction.	MRB price limits	At least 50% of the units must be affordable to low or moderate income for the period of any loan or 20 years, whichever is longer. Also required is a finding that a shortage of good housing exists for these income groups in the area.	All housing units within a development must be occupied by lower and very low income households.	All units constructed must be eligible for Agency end loan financing; Agency provides list of eligible municipalities.
Affordability requirements: Beneficiary	Rental: families earning 60% or less of area median income (AMI). Homeowner: families earning 90% or less of AMI. Rent/mortgage <= 30% of annual household income.	MRB income limits	Households with incomes at 80% or less of AMI.	Household income must be below 80% of AMI. Housing costs can be no more than 30% of one twelfth of the adjusted annual household income.	"Range of Affordability" as defined by Council on Affordable Housing used to determine regional median incomes.
Funding Source	State's general obligation bonds	By state statute, KHC is authorized to issue housing development fund notes to fund the HDF. No more than $5 million in fund notes or other borrowings shall be outstanding at any time.	Original state approp. of $4 million; $200-300k added yearly from fees paid to the Authority from the development of qualified residential rental projects financed by bonds issued prior to 1988.	20 cents increase in state stamp tax per $500 of real estate sold. It usually generates about $2 million per year.	Initial $45 million financed through spread on bond yields; 10/97, refinanced old bonds for an additional $10 million.

AFFORDABLE HOUSING INITIATIVES: CONSTRUCTION LOAN PROGRAMS

State	Mississippi	Kentucky	New Hampshire	South Carolina	New Jersey
Program Evaluation					
Production Statistics	Loans to Developers - 628 units / 34 loans (502 of the units are rental units); DPA loans - 1043 loans/units	Approx. 100/year; total 2000-2500	676 units since inception	1161 units (through 1994	59 developments/1647 units;
Cost-benefit	-for developer loan program - MAHDF$ - $10,408/unit ave.; Ave. total cost/unit - $60,427; Administrative Costs??			Funded an avg. of $6,797 per unit	Administrative costs covered primarily by lead lender;

Tax Abatement Programs

Tax abatement programs are designed to provide developers with all or partial relief from a tax obligation in return for provision of affordable housing as part of their development plans.

The first of these programs, and least likely to be replicated (for Tennessee, anyway), is the Virgin Islands Affordable Housing Program. Under the regulations pertaining to this program, interested developers must file an Affordable Housing Development Plan and a Certificate of Compliance with the development regulations with the Virgin Islands Housing Finance Agency. Developers who maintain compliance with the regulations receive tax exemptions as follows: 100% exemption on gross receipts taxes and on excise taxes on materials and supplies brought into the Virgin Islands and used exclusively in the production of affordable housing; 100% exemption on income taxes for the term of the applicable Affordable Housing Development Agreement for income derived from or effectively connected with the production of affordable housing. (The materials we received did not include the definition of affordable housing or if there were minimum percentages of a development that had to be affordable to become eligible for these benefits.)

The Neighborhood Assistance Program (NAP) administered by the State of Pennsylvania's Department of Community and Economic Development provides financial support for "a range of community-based programs" including housing rehabilitation and construction. Programs must serve persons who have low incomes (not exceeding 125% of federal poverty income guidelines) or are residents of impoverished neighborhoods. Businesses may either administer programs themselves or contribute money or in-kind resources to approved programs. In return, they are eligible to receive a 50 percent tax credit against state business and corporate net income taxes. A 70 percent tax credit is available for "Special Program Priorities" which currently include housing rehabilitation and construction. Current funding is for $16,750,000 in state tax credits.

The State of Indiana also has a Neighborhood Assistance Program (NAP) which provides state income tax credits for community and housing development. This program is regulated by the Indiana Department of Commerce. Considerably smaller than the Pennsylvania program, this program is limited to only $2.5 million in NAP credits annually. Also, for the Indiana program, applicants must be not-for-profit corporations. Private, for-profit businesses only play a role if they make a donation to the not-for-profit project, then they can take a credit for one-half of the amount donated, up to a maximum of $25,000.

The benefits of this type of program are that housing is provided by private, for-profit developers (in the first two instances) and that there is a direct cost incentive provided for the development of affordable housing. Such programs are relatively easy to establish and administer. The costs of the programs are measured by the extent of foregone revenues. In addition, these programs will only be effective at producing affordable housing to the extent that the tax obligation avoided more than outweighs the additional profits that a developer could realize by building more highly priced housing.

Other Programs

Besides these "groups" of incentive programs, we also received information on a few other unique programs. One of these was the Louisville Buyer Assistance Program in Kentucky. In conjunction with the Jefferson County Metropolitan Sewer District (MSD), KHC and the City of Louisville have developed this program which permits developers to pay funds into a special account maintained by the county in lieu of paying MSD's usual Sanitary Sewer Capacity Charges for certain housing defined as "affordable." The funds in the account are then used to make grants to homebuyers to cover a portion of the closing costs and downpayments on qualified housing purchases. To be included, homes and homebuyers must fall within the acquisition cost and income limits of KHC's MRB program. Grant assistance is currently about $936 at closing. Not all homes in a development are required to be "affordable." This plan is "cost neutral" to the developer, because he/she pays the same amount, just to a different recipient. However, the benefit to the developer is that the assistance will aid low to moderate-income buyers in purchasing homes and the availability of funds should increase the number of potential buyers for these homes.

Programs in the State of Connecticut

As requested by HJR 505, we looked specifically at affordable housing initiatives in the State of Connecticut, including the Housing Partnership Program and the Affordable Housing Land Use Appeals Process. While neither of these programs provides a direct financial incentive for development of affordable housing, both are designed to ease the procedural hurdles faced by developers who are interested in developing affordable housing and make them more aware of any assistance that may be available. The state housing partnership program was formed to encourage the formation of *local* housing partnerships. These local partnerships receive technical assistance from the State Department of Economic and Community Development (DECD), which includes the coordination and provision of information on resources of potential assistance and development of a local "housing strategy." Furthermore, the DECD gives these partnerships priority in funding for any available financial assistance, as does the State Department of Environmental Protection.

The Housing Land Use Appeals process provides that any person whose affordable housing application is denied or is approved with restrictions which have a substantial adverse impact on the viability of the development may appeal such decision to a special judge assigned to hear such appeals. The local commission who denied the application has the burden of proving that other public interests clearly outweigh the need for affordable housing and such public interests cannot be protected by reasonable changes to the affordable housing development.

Tennessee Growth Planning Legislation

In May of 1998, the State of Tennessee passed growth plan legislation that has provisions similar to the Connecticut program. Although not identical, both programs contain provisions which allow persons (developers in the case of the Connecticut program) and citizens (in the case of the Tennessee program) to appeal decisions by counties or cities which impact the land use in their area. Because the Tennessee program is new, no data or detailed analysis is provided in this report.

PART IV: Evaluation

This report has looked at a variety of affordable housing programs. Below, we provide an analysis of a selected number of these programs and their relevance to the State of Tennessee. Provided also is a historical context for the implementation and establishment of affordable housing programs.

Housing Market Conditions and Initiatives for Affordable Housing

When market-driven home construction failed to generate enough affordable housing for the low and moderate-income households, public officials sometimes found it necessary to intervene. Such state and local intervention strategies found very few takers in private, market-driven housing developments. However, such efforts have found some acceptance among homebuilders and wider support in the public arena when the following demographic and market trends existed:

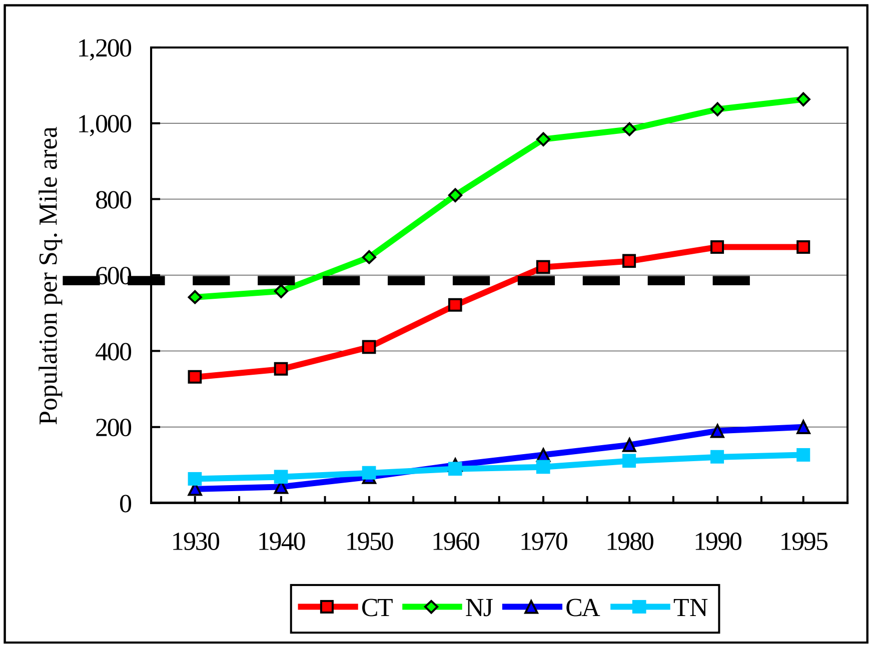
- *Population density had reached very high levels due to rapid population growth.*
- *The proportion of area farmland to the total land declined to a very low level.*
- *The price of farmland rose to very high levels, an indicator that land for new developments was at a premium.*

These three trends created market conditions that pushed up the costs of production and the market prices of homes beyond normal levels of affordability. In such circumstances, many public jurisdictions found it appropriate to relax zoning and subdivision regulations and to provide density bonus incentives in order to promote the private development of affordable homes.

Comparisons among Selected States

Three states that have had success with statewide actions to promote affordable housing include California, New Jersey, and Connecticut. New Jersey and Connecticut both reached statewide population density levels above 600 persons per square mile some time ago, with New Jersey exceeding the 1,000 mark by 1970. (See Chart 11) High levels of population density in these two states and the accompanying pressure on their housing markets made their intervention in the housing market necessary and timely.

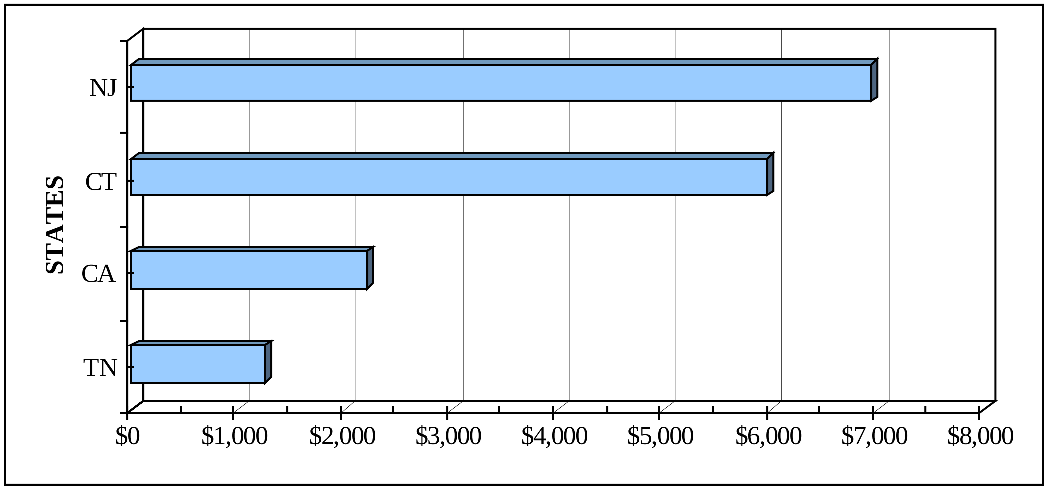
Chart 11. Comparison of Trends in Population Density California, New Jersey, Connecticut, and Tennessee



Source: THDA tabulations of "USA COUNTIES 1996, A Statistical Abstract Supplement" data, U.S. Department of Commerce, Economics and Statistics Administration, Bureau of the Census.

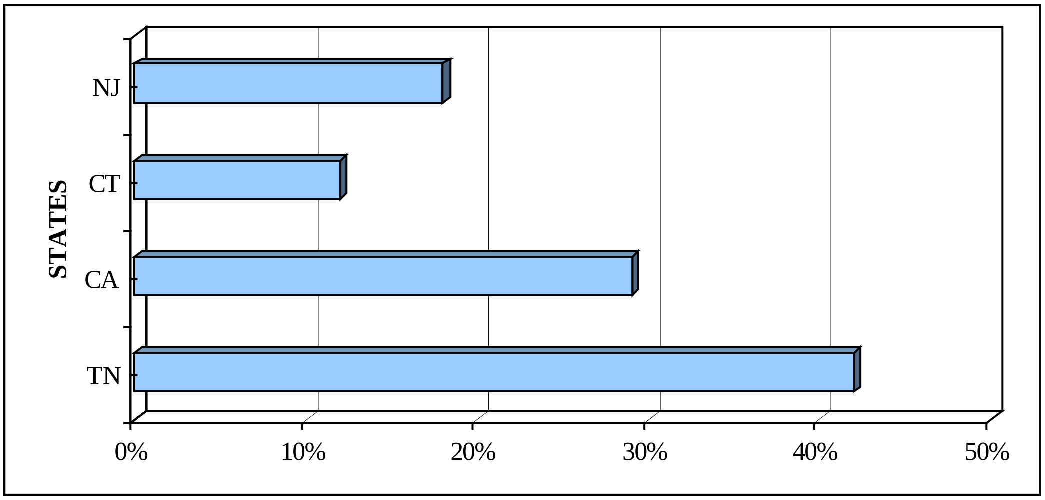
Connecticut and New Jersey also experienced relative scarcity and higher prices for land needed for new development (see Chart 12 and Chart 13). The fact that these pressures were not as widely spread out statewide may explain why California's state efforts to promote fair-share affordable housing encountered strong resistance and lost significant political support in recent years. Based on the past experience of these states and localities, it is natural to conclude that Tennessee has yet to undergo the intensive demographic and price pressures that warrant a statewide affordability initiative.

Chart 12. Average Value of Farmland & Building Per Acre in 1992



Source: THDA tabulations of "USA COUNTIES 1996, A Statistical Abstract Supplement" data, U.S. Department of Commerce, Economics and Statistics Administration, Bureau of the Census.

Chart 13. Percent of Land in Farms in 1992

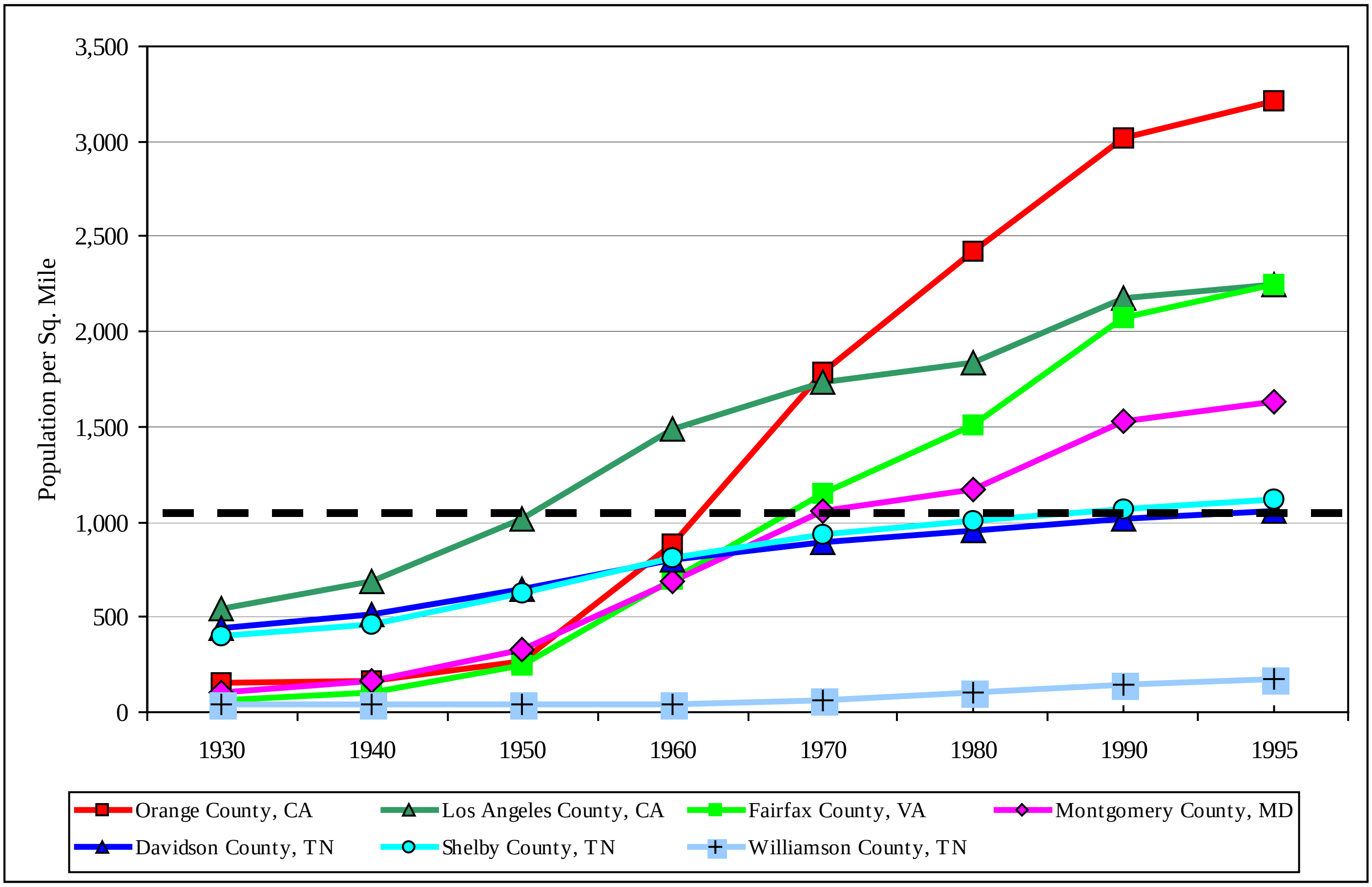


Source: THDA tabulations of "USA COUNTIES 1996, A Statistical Abstract Supplement" data, U.S. Department of Commerce, Economics and Statistics Administration, Bureau of the Census.

Comparisons among Counties

The four out-of-state counties included in Chart 14 (Montgomery, MD; Fairfax, VA; Los Angeles and Orange, CA) began important inclusionary housing programs well after they reached population densities above 1,000 per square mile and their efforts gained momentum as the densities continued to rise.

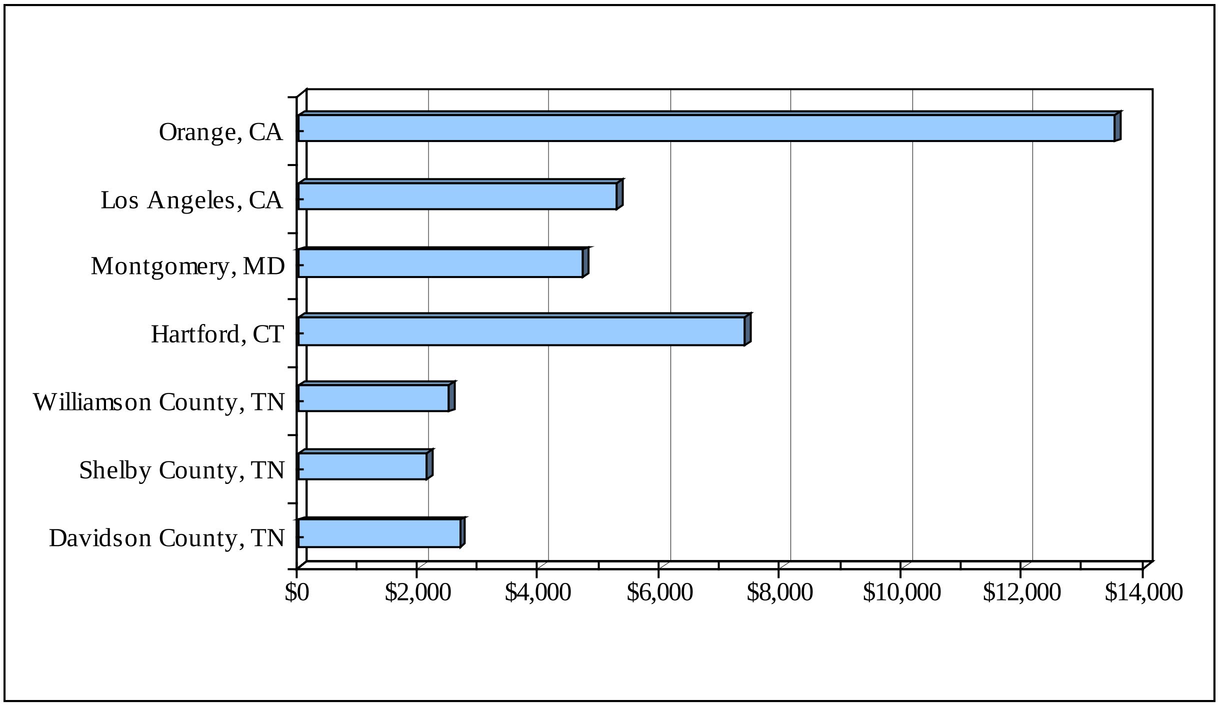
Chart 14. Comparison of Trends in Population Density
Shelby, Davidson & Williamson vs. Selected Out-Of-State Counties



Source: THDA tabulations of "USA COUNTIES 1996, A Statistical Abstract Supplement" data, U.S. Department of Commerce, Economics and Statistics Administration, Bureau of the Census.

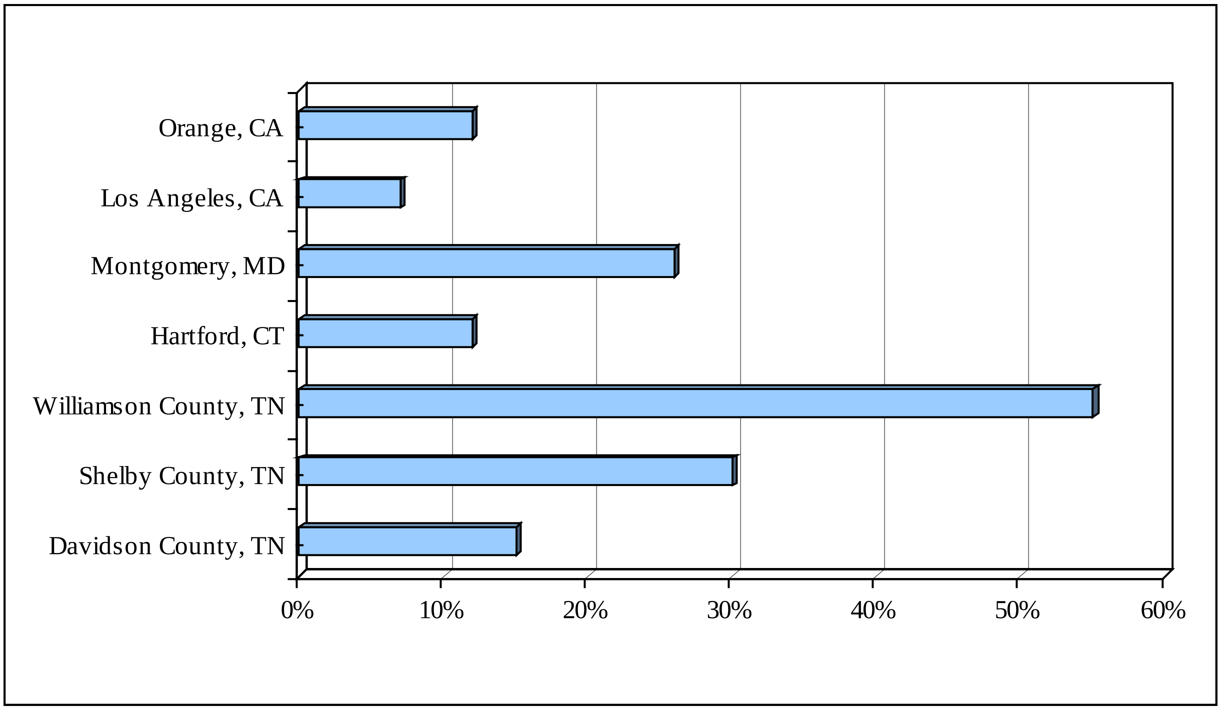
Only two Tennessee Counties, Davidson and Shelby, have crossed this density mark. Their density levels have risen at a much slower pace recently compared to the post-1970 density surges in the four out-of-state counties. In comparison with the same, Davidson and Shelby, as well as Williamson County, have the relative advantage of much lower land prices also. Census data indicate that only 12 of the 95 counties in Tennessee exceeded the average farmland value of $2,000 per acre in 1992, compared to 34 out of the 59 counties in California, a state close to Tennessee in overall population density.

Chart 15. Average Value of Farmland & Building Per Acre in 1992



Source: THDA tabulations of "USA COUNTIES 1996, A Statistical Abstract Supplement" data, U.S. Department of Commerce, Economics and Statistics Administration, Bureau of the Census.

Chart 16. Percent of Land in Farms in 1992

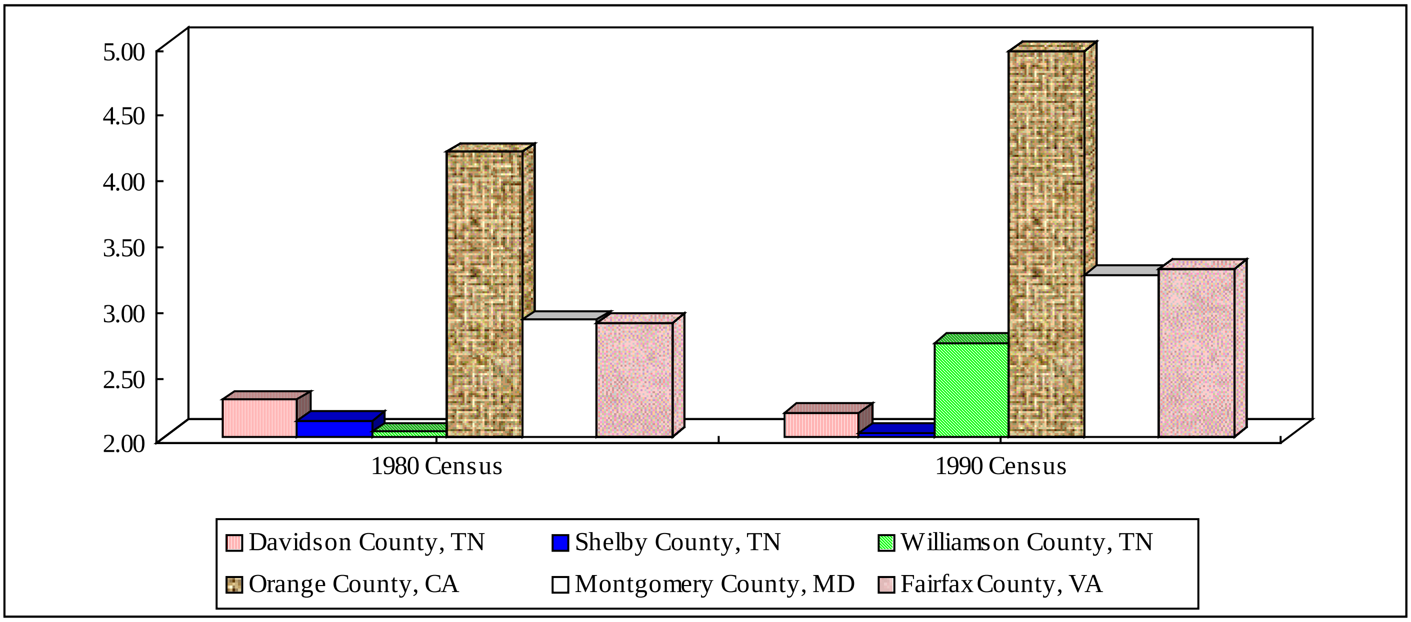


Source: THDA tabulations of "USA COUNTIES 1996, A Statistical Abstract Supplement" data, U.S. Department of Commerce, Economics and Statistics Administration, Bureau of the Census.

Affordability varies inversely to, and so can be inferred from, a simple ratio of median home value to median family income. For example, when this ratio has a high value 3, the home value is three times the median income, an indication that affordability is very low. From Chart 17, it is easy to observe that all three Tennessee counties were quite affordable in 1980, when both Montgomery, MD and Fairfax, VA already had ratios nearing 3 indicating low affordability levels at that time. In addition, affordability declined considerably in these two Washington metropolitan counties during the 1980s when Williamson County in Tennessee also lost important ground in affordability. During this decade, both Davidson and Shelby Counties in Tennessee maintained their comfortable affordability levels.

Chart 17. Ratio of Median Home Value to Median Family Income: 1980 & 1990

	1980 census			1990 census		
	Fam. Inc.	Hom. Val.	Ratio	Fam. Inc.	Hom. Val.	Ratio
Davidson County, TN	$19,733	$45,000	2.28	$34,785	$76,000	2.18
Shelby County, TN	$18,191	$38,600	2.12	$32,671	$66,500	2.04
Williamson County, TN	$23,617	$48,100	2.04	$48,332	$131,100	2.71
Orange County, CA	$25,918	$108,100	4.17	$51,167	$252,700	4.94
Montgomery County, MD	$33,702	$97,400	2.89	$61,988	$200,800	3.24
Fairfax County, VA	$33,173	$95,200	2.87	$65,201	$213,800	3.28

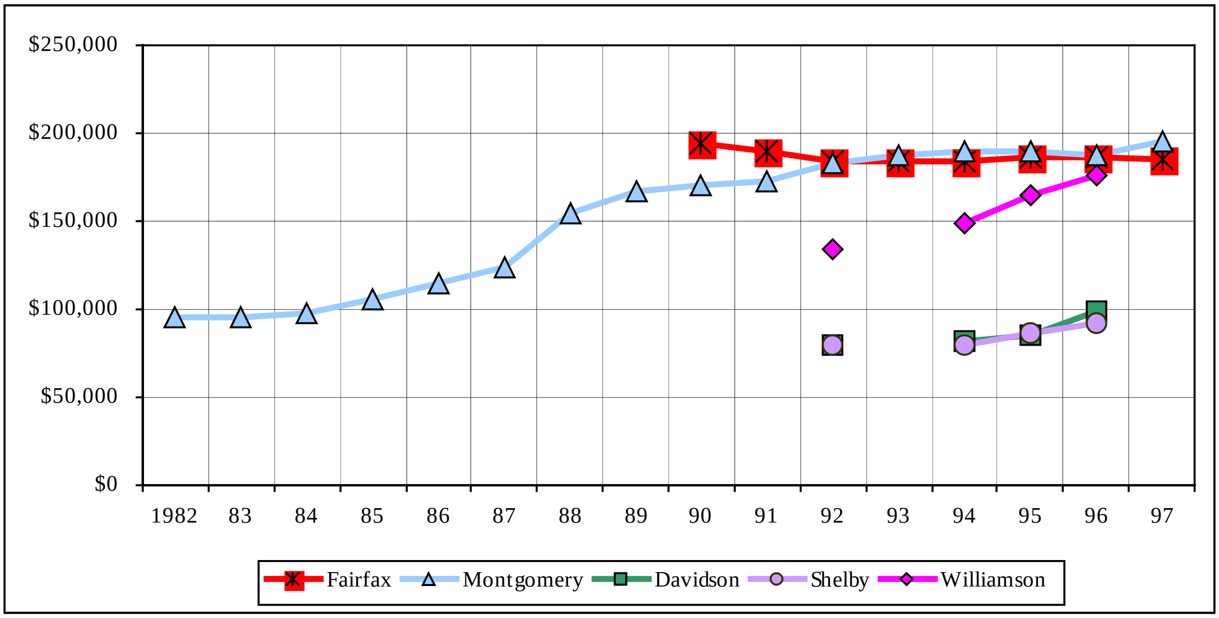


Source: THDA tabulations of "USA COUNTIES 1996, A Statistical Abstract Supplement" data, U.S. Department of Commerce, Economics and Statistics Administration, Bureau of the Census.

Home Sales Price Levels and Trends

Home prices have shown some stability in both Montgomery County and Fairfax County in recent years. The meager population increases in these two counties in recent years are mostly due to natural increase and immigration. A critical review of the inclusionary programs in Fairfax County is currently underway. Montgomery County exceeded the $100,000 median sales price level in 1984 and approached the $190,000 level in 1997. Fairfax County median home prices were hovering below the $190,000 level during the 1990s. Both Shelby County and Davidson County are below the $100,000 level, while Williamson County median prices are rapidly climbing towards the $180,000 mark, at an annual rate of seven percent.

Chart 18. Median Home Sales Prices



Source: THDA analysis of 1996 & 1997 Home Sales Price data maintained by the Property Assessment Division, Comptroller's Office, State of Tennessee. Fairfax County data obtained from: Fairfax County Office of Research and Statistics, Urban Development Information System, 1990 Parcel File. Montgomery County data tabulated by Montgomery County Department of Park and Planning, Research and Technology Center, using data provided by the Maryland State Department of Assessment and Taxation.

Some Local Efforts for Affordable New Construction

Given these findings, it is not surprising that serious concerns about housing affordability are rarely brought forth in local jurisdictions outside the Nashville and Memphis MSAs. As discussed in a previous section, Williamson County adopted a density bonus ordinance which included a "housing bonus" to encourage developers to construct housing affordable to persons with low and moderate-incomes, but has had little success as a result of it.

In Memphis, the City Council and the Shelby County Board of Commissioners adopted an ordinance in 1994 in an effort to promote affordable housing construction. The developer incentives in this case centered around savings in the infrastructure-related fees. Apparently, this program has not generated much interest among developers.

More recently, Nashville also passed a type of density bonus ordinance called a Development Bonus. The purpose of this bonus, however, is not solely to provide affordable housing. Additional density is allowed if dedicated for public use of land or of a site. The affordable housing provision allows for additional bonus within a planned unit development (PUD) with specifications based on the type of dwelling. The number of bonus units shall not exceed 10 percent of the total number of dwelling units/lots otherwise constructed for lease or sale at free market rates whether in a multifamily development or in a single family or two family development. The combined number of bonus units (multifamily) or lots (single family and two family) shall not exceed 10 percent of the total number of units/lots otherwise created. For example, where the number of units/lots totals 50, an additional 10 percent (five units/lots) shall be allowed for bonus units/lots. The five bonus units/lots would consist of three affordable housing units/lots and two market rate units/lots.

Due to the recent enactment of this provision, no data were available on the use of this provision by developers, nor on the amount of affordable housing created.

PART V: Comments. Concerns, and Suggestions

From the Home-building, Finance, and Real Estate Industries

While legislative mandates have led in many cases to the implementation of affordable housing programs in other areas of the country, Tennessee has attempted to address this issue, not through mandates, but through incentives for developers. The success or failure of such programs is dependent on a large number of factors and individuals involved in the process. For example, in areas where the affordable housing units are perceived as negative in their overall effect on a community's property value, opposition from homeowners and other residents can result in lawsuits and the emergence of "NIMBY", not in my back yard, attitudes. Furthermore, if developers are not willing to participate because of issues related to profitability, affordable housing programs might not work. In an effort to look comprehensively at this issue, we contacted a number of homebuilder associations to discuss the direct impact of affordable housing initiatives on them. The following summary attempts to articulate those issues or concerns of developers, home-builders, finance professionals, and those in the real estate industry, and gain a better understanding of the types of incentives that developers would respond positively to in the provision of affordable housing. This information was used to assist us in drawing some conclusions about the impact this might have on affordable housing legislation in the State of Tennessee.

Copies of this study were sent to homebuilder and Realtor® associations throughout the state and to other housing professionals, planners, housing organizations, and mortgage bankers associations. Each organization was asked to review, comment, and offer advice on incentives for creating affordable housing (their responses are included in the Appendix of this document). Other information and comments were received by phone or in person and are included in the summary provided below. Comments from these groups were used to help develop the framework for recommendations to be made to the General Assembly. Some general conclusions:

- Density bonus programs require specific conditions in order to be effective; in most areas of Tennessee, these conditions don't exist.

- Affordable housing depends in large part on government incentives on the local, state, and national level.

- Local governments need authority from the state to develop and implement many of the programs which might increase the availability of affordable housing. If local governments are to provide certain kinds of waivers of requirements or offer certain kinds of tax incentives, those should be authorized in state law.

PART VI: Recommendations and Suggestions for Legislative Action

While THDA conducted a comprehensive study based on the directives given by HJR505, our recommendations go beyond that specific charge:

- Any incentives authorized by the state should be flexible, allowing communities to address the lack of affordable housing based on their specific economic conditions, housing markets, and population density. Clearly, not all communities need density bonus programs because not all have problems with availability of land.

- Any planning done which looks at growth, annexation, and future land use should also include consideration of the direct and indirect costs and effects on the provision of affordable housing. Such planning should contain provisions to help provide affordable housing. The planning should also consider the impact and needs of businesses moving into the area, the skill level of employees needed, and whether there will be housing available which is affordable to them.

- More education is needed within communities so that residents understand that providing affordable housing does not threaten existing home values or contribute to neighborhood deterioration.

- Residents, businesses, home builders, Realtors®, housing professionals, government leaders, and others should work together to consider the many factors that affect housing affordability and try to find comprehensive solutions.

- More research should be done on how to best provide and pay for the infrastructure for increasing affordable housing.

- THDA should develop a comprehensive directory of successful affordable housing programs throughout the country. This directory should include specific details of how these programs work and which areas of Tennessee have economic, demographic, and market conditions which might be appropriate for successful replication of these programs. This directory should be easily available to government officials, businesses, professional organizations, and others interested in affordable housing.

- THDA should investigate development of a program which would provide encouragement to developers to build affordable housing, such as a construction loan program.

Endnotes

[1] See The Enterprise Foundation website at: www.enterprisefoundation.org

[2] Undated Report of the Maryland Department of Housing and Community Affairs, "The Moderately Priced Dwelling Unit Program".

[3] August 1993 Report of the Virginia Department of Housing and Community Development, "Affordable Housing Density Bonus Ordinances".

[4] Unless otherwise noted, all information regarding inclusionary housing programs in California was taken directly from "Inclusionary Housing in California and New Jersey: A Comparative Analysis", Nico Calavita, Kenneth Grimes, and Alan Mallach; HOUSING POLICY DEBATE, Volume 8, Issue 1.

[5] Robert White, *Fairfax Journal*. "Supes Update Low-Cost Housing Policy", March 31, 1998.

[6] Williamson County Zoning Ordinance, Section 5310 Housing Bonus.